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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

THE DON'T BANKRUPT WASHINGTON COMMITTEE,
Appellant,

v.

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO, SEATTLE-FIRST NATIONAL BANK, MORGAN GUARANTY TRUST COMPANY OF NEW YORK, and THE UNITED STATES OF AMERICA,
Appellees.

On Appeal From the United States Court of Appeals for the Ninth Circuit

MOTION OF APPELLEES SEATTLE-FIRST NATIONAL BANK AND MORGAN GUARANTY TRUST COMPANY OF NEW YORK TO DISMISS OR AFFIRM

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QUESTIONS PRESENTED

1. Whether a municipal corporation's covenants to complete construction of energy generating facilities, made to holders of bonds payable from the revenues of those facilities, are substantially impaired by a state statute that conditions compliance with those covenants on the results of a popular referendum?

2. Whether a state statute that substantially impairs a municipal corporation's covenants by subjecting them to the electorate's veto violates the Contract Clause of the United States Constitution because it is not a reasonable and necessary means to serve a legitimate public purpose?

LIST OF PARENT COMPANIES, SUBSIDIARIES AND AFFILIATES

Seattle-First National Bank ("Seattle-First") is a wholly owned subsidiary of Seafirst Corporation. All of Seattle-First's subsidiaries are wholly owned, excluding director qualifying shares in certain instances. In addition, Seattle-First has no affiliates other than those wholly owned by its parent, Seafirst Corporation, or by one of its parent's wholly owned subsidiaries. Should the Court desire disclosure of these companies, Seattle-First will supplement its list of subsidiaries and affiliates.

Morgan Guaranty Trust Company of New York ("Morgan Guaranty") is a wholly owned subsidiary of J.P. Morgan & Co., Incorporated. Morgan Guaranty's subsidiaries (except wholly owned subsidiaries) are: Banco Morgan Finansa and Bank Morgan Labouchere N.V. Eleven subsidiaries are wholly owned by Bank Morgan Labouchere N.V. Morgan Guaranty has no affiliates other than those wholly owned by its parent, J. P. Morgan & Co., Inc., or by one of its parent's wholly owned subsidiaries. Should the Court desire disclosure of these companies, Morgan Guaranty will supplement its list of subsidiaries and affiliates.

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MOTION OF APPELLEES SEATTLE-FIRST NATIONAL BANK AND MORGAN GUARANTY TRUST COMPANY OF NEW YORK TO DISMISS OR AFFIRM

Appellees Seattle-First National Bank and Morgan Guaranty Trust Company of New York (the "Trustees") respectfully move to dismiss this appeal or, in the alternative, to affirm the judgment of the court of appeals. Supreme Court Rule 16.1(c) and (d).

OPINIONS BELOW

The court of appeals' opinion (J.S. App. 1a-20a)[1] is reported at 696 F.2d 692. The district court's opinion (J.S. App. 21a-23a) is not reported.

JURISDICTION

The court of appeals entered judgment on January 11, 1983. The State of Washington, an appellant before the court of appeals, elected not to seek review by this Court. Appellant The Don't Bankrupt Washington Committee filed its jurisdictional statement on February 25, 1983, invoking this Court's jurisdiction under 28 U.S.C. 1254(2). As is more fully discussed in the Motion of Appellee Continental Illinois National Bank and Trust Company of Chicago to Dismiss or Affirm, however, appellant lacks standing to invoke the Court's appellate jurisdiction.

STATEMENT

The Washington Public Power Supply System (the "Supply System") is a municipal corporation and "joint operating agency" of the State of Washington. It comprises 19 public utility districts and four cities, all of which are also Washington municipal corporations. The Supply System is authorized by statute to construct and operate electric power plants and to issue revenue bonds to finance their construction. RCW 43.52.300; RCW 43.52.3411. Pursuant to that authority, it is currently building three nuclear power plants ("Projects 1, 2 and 3").[2]

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[1] References to the Jurisdictional Statement and its Appendix will be designated "J.S." and "J.S. App." The designation "Ex." refers to Exhibits, which were not given Clerk's Record numbers. The Clerk's Record is abbreviated "CR," and citations to the Amended Pretrial Order will be in the form "PTO," followed by the relevant paragraph number. The abbreviation "RP" refers to the report of proceedings before the district court.

[2] The Supply System in 1981 terminated construction on two other plants. They are not at issue in this case.

On November 3, 1981, Washington's voters passed Initiative 394, RCW Ch. 80.52 (the "Initiative"). The Initiative prevents the Supply System from issuing or selling bonds to finance completion of Projects 1, 2 and 3 without first obtaining authority in a popular election. Before passage of the Initiative, Washington law did not require direct voter approval for the issuance and sale of Supply System bonds, or for the expenditure of their proceeds.

This case involves the constitutionality of the Initiative as applied to the Supply System's contracts with the holders of revenue bonds previously issued to finance construction of Projects 1, 2 and 3. These bonds were issued and sold pursuant to a master Bond Resolution for each project.[3] Under Washington law, each Resolution is a contract between the Supply System and the purchasers of the billions of dollars of bonds issued to finance these projects. RCW 54.24.110; *see also* Res. 640 and 775, § 14.1 (Ex. 9, 10); Res. 769, § 15.1 (Ex. 8).

Bond purchasers require more than a simple promise of repayment. They therefore obtain additional security for their investment, which takes the form of covenants either requiring or limiting the issuer's actions. In this case, the bonds are revenue bonds, payable solely from income derived by the Supply System through its ownership and operation of each project. PTO (CR 170) ¶ 64. Because completed projects will produce electricity which can be sold to help generate income, the Supply System covenanted with bond purchasers that it

[3] Seattle-First, by the terms of Resolution 775, is Trustee for the holders of Project 3 bonds. Morgan Guaranty is Trustee for the holders of Project 1 bonds under Resolution 769. Under Resolution 640, Continental Bank is Trustee for the holders of Project 2 bonds and has filed, under separate cover, its own Motion to Dismiss or Affirm. The contractual obligations relating to the three projects are substantially the same and therefore will be discussed as a group.

could issue bonds to complete each project,[4] that it *would* issue and sell additional bonds in amounts sufficient to complete each project,[5] and that it *would* "construct [each project] to completion."[6] The covenant to complete was subject to one primary exception—the projects would not be completed if the Supply System and the Bonneville Power Administration ("Bonneville") jointly determined that the projects could not produce electricity consistent with Prudent Utility Practice, or, if they

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[4] Each Resolution provides, in the article entitled "COVENANTS TO SECURE BONDS":

> *Protection of Security.* The System is duly authorized under all applicable laws to create and issue the Bonds and to adopt this Resolution and to pledge the revenues and other moneys, securities and funds purported to be pledged by this Resolution in the manner and to the extent provided in this Resolution. (Res. 640 § 9.14; Res. 769, § 10.15; Res. 775 § 9.13) (Exs. 9, 8, 10).

The "Bonds" include *all* bonds "issued pursuant to the terms, conditions and limitations of [each] Resolution in series, in such amounts, and from time to time, as may be required to pay the Cost of Construction. . . ." Res 640 and 775, § 3.1 (Exs. 9, 10); Res. 769, § 4.1 (Ex. 8). Thus, the covenant of authority to issue "the Bonds" extends to bonds not yet issued, but which *will* be issued to pay "Costs of Construction."

[5] The Resolutions contain the following promise:

> The System hereby covenants and agrees that it will take all lawful measures required to issue and sell from time to time or at one time additional Series of Bonds to the extent required to enable the System to pay the remaining balance of the Costs of Construction. (Res. 640 and 775, § 3.4; Res. 769, § 4.4.) (Exs. 9, 10, 8).

[6] In each Resolution, the *first* covenant in the article entitled "COVENANTS TO SECURE BONDS" is to complete the project:

> The System will, subject to the provisions of the Project Agreement, (i) proceed with all reasonable diligence to and *will construct to completion* the Project and complete such construction at the earliest practical time . . . . (Res. 640, § 9.1; Res. 769, § 10.2; *see* Res. 775, § 9.1.) (Exs. 9, 8, 10) [Emphasis Added.]

In the case of Project 3, the covenant to complete is also subject to the Ownership Agreement. Res. 775, § 9.1 (Ex. 10).

disagreed, an independent consultant so determined.[7] On the strength of these promises, approximately $4.5 billion of Project 1, 2 and 3 bonds were purchased prior to the Initiative's passage. *See* PTO (CR 170) ¶¶ 87-89.

The Initiative cuts the contractual knot binding the Supply System and its lenders. The Supply System's covenants are now subject to a plebiscite, and it can issue additional bonds to complete construction *only* if the voters approve, irrespective of whether completion is required under the Bond Resolutions.

The primary question in the case, then, is whether the Supply System's bondholders, having lent more than $4,500,000,000 to a Washington municipal corporation, are entitled to the security that they bargained for. The district court found that they are, and the court of appeals agreed.[8] The State of Washington and several of its elected officials were parties in the courts below; they do not, however, seek to overturn the lower courts' decisions.

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[7] The Project 1 and 2 Agreements provide for termination of the Project when:

> (b) The parties [Bonneville and the Supply System] determine the Project is not capable of producing energy consistent with Prudent Utility Practice or, if the parties disagree, the Project Consultant so determines .... (Project 1 and 2 Agree. § 15(b).) (Exs. 1,2).

Prudent Utility Practice requires that the Project be completed if completion can be

> expected to accomplish the desired result at the lowest reasonable cost consistent with reliability, safety and expedition. (Project 1 Agree., § 1(p) (Ex. 1); Project 2 Agree., § 1(k) (Ex. 2).

Provision for determination of disputes by the Consultant is found in Section 10. Similar provisions for Project 3, which has a private ownership component, are found in Sections 3, 4 and 7 of the Ownership Agreement (Ex. 4). Provision for terminating Project 3 when completion is not consistent with Prudent Utility Practice appears at Section 22(a) of the Ownership Agreement (Ex. 4).

[8] The Trustees also contended that the Initiative's voting scheme violated the Equal Protection Clause and the Supremacy Clause of the United States Constitution, as well as provisions of the Washington Constitution. Resting their decisions solely on the Contract Clause, neither the district court nor the court of appeals addressed these claims.

ARGUMENT

The Trustees move to affirm the judgment of the court of appeals that Initiative 394, as applied to Projects 1, 2 and 3, violates the Contract Clause of the United States Constitution (Art. I, § 10, cl. 1). Alternatively, the Trustees move to dismiss the appeal on the ground that appellant lacks standing to invoke this Court's appellate jurisdiction.

The district court and court of appeals carefully applied the principles of *United States Trust Company of New York v. New Jersey*, 431 U.S. 1 (1977), to this closely analogous case. Because this Court's recent decision in *Energy Reserves Group v. Kansas Power & Light Co.*, 51 U.S.L.W. 4106 (Jan. 24, 1983), demonstrates its continued adherence to the standards enunciated in *United States Trust Co.*, the questions raised by this appeal are so foreclosed by this Court's prior decisions as to leave no room for controversy.

A. THE DISTRICT COURT AND COURT OF APPEALS CORRECTLY DETERMINED THAT INITIATIVE 394 SUBSTANTIALLY IMPAIRS THE SUPPLY SYSTEM'S CONTRACTUAL OBLIGATIONS TO BONDHOLDERS.

Because it would permit the Supply System to terminate Projects 1, 2 and 3 in circumstances not contemplated by the Bond Resolutions, the district court and court of appeals found that Initiative 394 effects a "severe impairment that defeats the expectations of the parties under their contracts." J.S. App. 15a (citation omitted); J.S. App. 22a. The Supply System and Bonneville have determined that completion of the three projects is consistent with Prudent Utility Practice, and additional bonds must be issued for completion to occur. *See* Squire Aff. (CR 72), ¶¶ 5, 18; Gjelde Aff. (CR 164), ¶¶ 8, 18. Therefore, were it not for the Initiative, the Supply System would have the unconditional obligation to sell bonds to complete the projects. Under the Initiative, however, the Supply System must submit a proposed bond sale for the completion of the projects to voters, who may reject it even though completion is consistent with Prudent Utility Practice as determined under the contracts. The

Initiative, then, eliminates the contractual standard governing the Supply System's obligation to issue the bonds and complete the projects, and transforms that standard into a political question subject to the vagaries of a popular referendum.

In concluding that Initiative 394 thus impairs the bondholders' contracts, the court of appeals engaged in a straightforward application of *United States Trust Co., supra,* 431 U.S. 1. There, the Port Authority of New York and New Jersey had issued and sold revenue bonds to pay for transportation projects. Part of the bonds' security was a covenant that precluded the Authority from spending revenues on mass transit projects which were not self-supporting. After several million dollars of bonds had been sold, the covenant was repealed.

New Jersey argued that the covenant's repeal did not lessen the bonds' security. The bonds retained an "A" rating, and, although bond prices dropped after the repeal, they regained their position in the market. *Id.* at 19, 43. Furthermore, the trial court found that, since the enactment of the covenant, the bondholders' security had been "substantially augmented by a vast increase in Authority revenues and reserves" (*Id.* at 42), and that various other security provisions protected the bondholders even after the repeal. *Id.* at 44. Notwithstanding substantial uncertainty as to whether the bondholders' security had been diminished, this Court held that the bondholders' contractual rights had been impaired:

> The fact is that no one can be sure precisely how much financial loss the bondholders suffered. Factors unrelated to repeal may have influenced price. In addition, the market may not have reacted fully, even as yet, to the covenant's repeal, because of the pending litigation and the possibility that the repeal would be nullified by the courts.
>
> In any event, the question of valuation need not be resolved in the instant case because the State has made no effort to compensate the bondholders for any loss sustained by the repeal. As a security

> provision, the covenant was not superfluous; it limited the Port Authority's deficits and thus protected the general reserve fund from depletion. Nor was the covenant merely modified or replaced by an arguably comparable security provision. Its outright repeal totally eliminated an important security provision and thus impaired the obligation of the States' contract. (*Id.* at 19; footnote omitted; citations omitted.)

The bondholders in this case are also the victims of a "repeal." Initiative 394 abrogates the Supply System's authority and obligation to issue additional bonds to complete the projects when consistent with Prudent Utility Practice. Moreover, under the Initiative the projects can be terminated simply because the voters disapprove of their completion. By thus permitting an action previously proscribed by the contracts, the Initiative's very existence substantially impairs the protection provided by the covenants to complete, regardless of whether the electorate ultimately prevents the sale of additional bonds. *See, e.g., id.* at 20-21 (State law which "permits a diminution of . . . pledged revenues and reserves" impairs covenant prohibiting such diminution). Nothing in the Initiative compensates the bondholders for their loss of this "important security provision." *Id.* at 19.

By thus impairing the bondholders' security, the Initiative "defeats the expectations of the parties under their contracts." J.S. App. 15a (citation omitted). This distinguishes the cases relied upon by appellant, where state statutes eliminated unforeseen windfall benefits without affecting the reasonable expectations of the contracting parties. In *City of El Paso v. Simmons*, 379 U.S. 497 (1965), for example, the Court found that a statute which restricted contracting parties "to those gains reasonably to be expected from the contract" did not effect a substantial impairment. 379 U.S. at 515; *see United States Trust Co., supra*, 431 U.S. at 31 (discussing *Simmons*). Similarly, in *Energy Reserves Group v. Kansas Power & Light, supra*, federal natural gas deregulation would have resulted in

windfall gains to natural gas producers. The price limitations imposed by the Kansas legislature eliminated only a portion of the windfall, still leaving producers in a better position than their contracts had contemplated:

> If deregulation had not occurred, the contracts undoubtedly would have called for a much smaller price increase than that provided by the Kansas Act's adoption of the § 109 ceiling. (51 U.S.L.W. at 4110).

Because the challenged statute permitted an even greater price for natural gas than the contracts envisioned, the producers' expectations were not violated.

In this case, however, the Initiative does not eliminate a mere unforeseen windfall benefit. It instead abrogates the exact performance originally envisioned. The completion covenants were designed to assure bondholders that termination would not occur based solely on one contracting party's judgment of Prudent Utility Practice—or, for that matter, the decision of an electorate not bound by the contractual standards. Bondholders were entitled to expect that decisions regarding continuance of the projects would be made in conformity with the contracts. These covenants take on even greater importance when, as the Initiative evidences, the projects are politically unpopular. The court of appeals was thus clearly correct under the standards of *Energy Reserves Group* and *United States Trust Co.* in affirming the district court's finding that Initiative 394 thwarted the bondholders' expectations.

These expectations, engendered by the covenants to complete, were "not superfluous." *See United States Trust Co., supra,* 431 U.S. at 19. Indeed, the undertakings impaired by the Initiative were a "central aspect" of the Supply System's contracts. J.S. App. 11a.[9] The Bond Resolutions themselves represent that the operation of each project is "essential to the

[9] A representative of one of the Supply System's largest bondholders testified that the covenants to complete are "extremely important," and that his company would not have purchased Project 1, 2 or 3 bonds had the issuance of additional bonds been subject to voter approval. Bates Dep. (CR 132), p. 15.

payment and security of the Bonds." *See, e.g.*, Ex. 10, § 11.1 (Bond Res. 775 Project 3); J.S. App. 11a; n.11. Notwithstanding the existence of other security, "completion of the plants unquestionably will make more energy available to finance repayment." *Id.; see* O'Brien Dep. (CR 146), p. 154; Bates Dep. (CR 132), pp. 11-13; Sitzer Dep. (CR 188), p. 137.

Furthermore, the Supply System's promise to finance "the plants to completion, subject only to contractually specified conditions . . . was clearly an inducement to contract." J.S. App. 16a (citations omitted). Each Official Statement issued by the Supply System in connection with its bond sales disclosed the Supply System's covenant to "complete construction of [each] Project at the earliest practicable time," and noted that the revenue bonds were to be paid solely from the "income, revenues, receipts and profits derived by the Supply System through the ownership and operation by it of [each] Project." *See* Ex. 77 (Sept. 1, 1975, Official Statement for Project 1 Bonds, Series 1975), pp. 37, 11.

Under the principles of *United States Trust Co.*, nothing more is necessary to establish the Initiative's substantial impairment of contract. Going further than the bond trustee in that case, however, the Trustees here proved that the Initiative was a primary reason for a downgrade in the bond rating of Project 1, 2 and 3 bonds.[10] *Compare United States Trust Co., supra*, 431 U.S. at 19, 44, n.12. The Trustees also showed, and the district court found, that the secondary market for the bonds fell as a direct result of the Initiative's passage.[11] RP 224 (J.S. App. 22a); *compare United States Trust Co., supra*, 431 U.S. at 19, 43. The finding of substantial impairment is thus supported by substantial evidence and must be accepted for purposes of the appeal.

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[10] *See* Ex. 48, Ackerman Dep. (CR 133), pp. 45-46, 48 (discussing downgrade by Moody's Investor Service); Ex. 54A (discussing downgrade by Merrill, Lynch).

[11] *See* Ex. 36M, 360 (CR 148); Ex. 82; Scholes Dep. (CR 147), p. 71.

B. THE COURTS BELOW CORRECTLY DETERMINED THAT THE CONTRACTS DID NOT RESERVE TO THE STATE THE POWER TO ALTER THE SUPPLY SYSTEM'S OBLIGATIONS.

> The court of appeals held that the contracts could not reasonably be read as contemplating the kind of alteration of WPPSS's bonding authority effected by Initiative 394. (J.S. App. 10a.)

The trial court reached the same conclusion. *See* RP 100. In coming to this result, both courts below correctly applied principles established by this Court.

1. To Be Effective, a Contractual Reservation Must be Clear and Explicit.

Municipal bond contracts "have the same meaning as contracts between private persons." *Murray v. Charleston*, 96 U.S. 432, 445 (1878), *quoted with approval in United States Trust Co., supra*, 431 U.S. at 25, n.23. A promise in a bond contract accompanied by a reserved right to "change the effect of the promise, is an absurdity." *Id.* Accordingly, when a state claims a reserved right to alter its contractual obligations, the express reservation "must be clear and explicit." *Owensboro v. Cumberland Telephone & Telegraph*, 230 U.S. 58, 71-75 (1913). The court of appeals correctly recognized this standard, holding that "reservations are not to be lightly inferred." J.S. App. 12a (citations omitted).

Appellant's suggestion that the Supply System's obligations should instead be construed strictly against the bondholders, who have loaned $4.5 billion on the strength of the contracts, is devoid of merit. *See* J.S. 15-16. This Court has construed contracts in favor of the State only where the contract evidences a grant by the sovereign. *See, e.g., Charles River Bridge v. Warren Bridge*, 36 U.S. (11 Pet.) 420, 544 (1837) (franchise); *Northwestern Fertilizing Co. v. Hyde Park*, 97 U.S. 659, 666 (1878) (corporate charter). The Bond Resolutions, however, grant no privilege to the bondholders. On the contrary, they provide for repayment of and security for the bondholders' loans. In these circumstances, strict construction

of the Supply System's obligations against its creditors would be both unprecedented and unjust.[12]

2. RCW 43.52.3411 Does Not Reserve to the State the Power to Amend the Bondholders' Contracts.

RCW 43.52.3411 authorizes a joint operating agency to issue revenue bonds "by resolution" whenever it "shall deem it advisable." J.S. App. 33a-34a. The form, content and legal effect of bonds so issued, as well as the procedures for their issuance, are governed by "the provisions of law as now or hereafter in effect relating to revenue bonds of public utility districts." *Id.* at 34a. The court of appeals concluded that this incorporation by reference of statutes relating to Washington public utility districts ("PUDs") did not constitute "a reservation of state authority to make the changes imposed by Initiative 394." J.S. App. 12a-13a.[13]

A study of predecessor statutes to RCW 43.52.3411 establishes that the court of appeals correctly identified its purpose.[14] In 1955, Washington enacted detailed legislation governing the

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[12] *Keefe v. Clark*, 322 U.S. 393 (1944), does not bear upon this issue. This Court there held only that it would not interpret a state statute to create a contractual obligation absent evidence of the legislature's clear intent to do so. 322 U.S. at 396-7. Here, no one questions the existence of the contractual obligations. *See* J.S. 12, n.12; PTO (CR 170) ¶¶ 61-63.

[13] Appellant has also claimed that Section 5(a) of the Project Agreements reserves the State's right to curtail the Supply System's authority to issue additional bonds. Even if that is the case, the reservation is ineffective against bondholders, who were not party to the Project Agreements. Indeed, appellant makes no claim that the alleged reservation in Section 5(a) of the Project Agreements affects the bondholders' rights. *See* J.S. 13 (Section 5(a) "constitutes a clear warning to BPA . . .").

[14] Appellant implausibly argues that the purported reservation in RCW 43.52.3411 was enacted because of the abolition of the Washington State Power Commission. J.S. 14, n.14. The only authority ever exercised by that Commission over joint operating agencies was its power to approve their construction of power projects. 1953 Wash. Laws Ch. 281, § 16. The Commission had no control over the issuance of bonds to complete the projects. *Id.* at § 15. Moreover, the legislature repealed the Commission's approval authority two years before enacting RCW 43.52.3411, suggesting the absence of a causal relationship between the two actions. 1955 Wash. Laws Ch. 258, § 17; 1957 Wash. Laws Ch. 295, § 6.

form, content and legal effect of joint operating agency bonds. These provisions were virtually identical to statutes controlling revenue bonds issued by public utility districts. *Compare* 1955 Wash. Laws Ch. 258, §§ 6-16 (governing joint operating agency bonds) *to* 1941 Wash. Laws Ch. 182, §§ 1-11 (governing PUD bonds, codified at RCW 54.24.020-120). To avoid unnecessary repetition, the legislature in 1957 repealed the duplicative statutes relating to joint operating agency bonds (with the exception of RCW 43.52.343, which differed slightly from RCW 54.24.060, the comparable PUD provision), replacing them with what is now RCW 43.52.3411. 1957 Wash. Laws Ch. 295, §§ 6, 7, 9. Thus, the language of RCW 54.24.030-050 and RCW 54.24.070-120, which had previously been set out in full, was incorporated into Chapter 43.52 by reference.

Viewed in this context, RCW 43.52.3411 is plainly a "reference" statute, designed solely "to avoid encumbering the statute books by unnecessary repetition . . ." *Knowles v. Holly*, 82 Wash.2d 694, 700, 513 P.2d 18 (1973). The phrase "as now or hereafter in effect" merely assures that Supply System and PUD bonds will continue to be equivalent in form and effect, notwithstanding future amendments to PUD bond statutes.[15] The purpose of RCW 43.52.3411 is thus simply to save space in the statute books, not to avoid the Contract Clause.

Furthermore, the very provision alleged to constitute an express reservation assumes that the Supply System has, and will continue to have, authority to issue bonds. That authority is expressed in the first two sentences of RCW 43.52.3411, which give the Supply System power to issue bonds "by resolution," whenever it deems issuance advisable. This aspect of Supply System authority is neither modified nor governed by

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[15] This equivalence also demonstrates that RCW 43.52.3411 reserves nothing to the State. The language that purportedly constitutes an "express reservation" does not appear in the statutes relating to PUD bonds. Construing RCW 43.52.3411 as reserving to the State the power to alter the Supply System's contractual obligations to bondholders would therefore violate the clear legislative intent to place the bonds of PUD's and joint operating agencies on an equal footing.

the "provisions of law as now or hereafter in effect relating to revenue bonds . . . of public utility districts." Consequently, the PUD bond statutes apply to "revenue bonds . . . *issued* by the joint operating agency." RCW 43.52.3411 (emphasis supplied).

The court of appeals thus correctly concluded that "the effect of Section 3411 simply is to render applicable to future bond issues the requirements of state law then in existence so long as" imposition of new requirements does not offend the Contract Clause. J.S. App. 13a.[16] This construction of a Washington state statute by the lower courts should be accepted on appeal. *See Huddleston v. Dwyer,* 322 U.S. 232, 237 (1944) (Court ordinarily accepts a "considered determination of questions of state law by the intermediate federal appellate courts").

C. THE COURT OF APPEALS CORRECTLY CONCLUDED THAT THE CONTRACTS DO NOT COMPEL THE STATE TO SURRENDER ESSENTIAL ATTRIBUTES OF SOVEREIGNTY.

This Court has frequently recognized the power of a municipality to covenant to exercise authority granted to it by the State, and has also held that the Contract Clause prohibits a state from impairing such promises. Thus, where a state authorizes a municipality to tax, and the municipality has promised, as security to creditors, to levy certain taxes, the Contract Clause precludes the State from withdrawing the power to tax until the obligation is satisfied. *Louisiana ex rel. Hubert v. New Orleans,* 215 U.S. 170 (1909); *Wolff v. New Orleans,* 103 U.S. 358 (1881); *Von Hoffman v. City of Quincy,* 71 U.S. (4 Wall.) 535 (1867); *see also United States Trust Co.,*

[16] Even if this conclusion were incorrect, summary affirmance or dismissal would remain appropriate. Because the reservation, if any exists, appears only in the Supply System's enabling statutes, it would preclude only the Supply System itself from complaining about a legislative change. It would not permit impairment of the Supply System's contractual obligations to third parties, such as bondholders. *Coombes v. Getz,* 285 U.S. 434, 440-42 (1932).

supra, 431 U.S. at 24, n.22. These cases rest upon the sound principle that "security" offered by a municipal corporation cannot be withdrawn. *Louisiana v. Pilsbury*, 105 U.S. 278, 288 (1882).

Washington has authorized the Supply System to construct generating facilities, issue bonds and make covenants "to protect and safeguard the security . . . of the holders thereof." RCW 43.52.300(2); RCW 43.52.3411; RCW 54.24.050. As security to the purchasers of billions of dollars of its bonds, the Supply System promised to complete its projects and to issue additional bonds as necessary for that purpose. It had the statutory authority to make these promises, and they therefore were not invalid *ab initio*. *See County of Moultrie v. Rockingham Ten-Cent Savings Bank*, 92 U.S. 631, 632-33 (1876); *see also United States Trust Co., supra*, 431 U.S. at 25 (revenue bond could be secured by "promise to continue operating the facility in question").

The Initiative now conditions performance of the covenants on the results of a vote. That this is a fundamental alteration of the Supply System's substantive obligation to bondholders, rather than a mere change in its governance, is illustrated by *Shapleigh v. City of San Angelo*, 167 U.S. 646 (1897). In *Shapleigh*, a court invalidated the City's incorporation after it had issued bonds. It then reincorporated. When bondholders sought to recover on the bonds, the new City relied upon a Texas statute, enacted after the bonds' issuance, which exempted a reincorporated municipality from liability on its predecessor's obligations unless they were assumed by a vote. This Court found that, if applicable to the facts before it, the statute would impair the bondholders' contract:

> If the law . . . was that, by a voluntary reincorporation and a taking over of property rights of the old corporation, the existing obligations devolved upon the new corporation, *it would plainly not be a legitimate exercise of legislative power, as affecting such prior obligations, to substitute an obligation contingent upon the vote of the taxpayers.* (167 U.S. at 657; emphasis supplied.)

The statute in *Shapleigh* thus impaired the City's obligation in the same way that Initiative 394 impairs the Supply System's obligation: the Initiative "substitute[s] an obligation contingent upon a vote" for the Supply System's contractual duty to complete the projects.

The Initiative's substantive effect is also illustrated by its abrogation of contractual standards. The Resolutions require completion unless the Supply System and Bonneville, or, if they disagree, an independent arbiter, determine that completion is inconsistent with Prudent Utility Practice.[17] But Initiative 394 does not, and could not, require voters to follow the Prudent Utility Practice standard:

> Initiative 394 adds a new and unpredictable element. . . . No standard can be imposed on the electorate in exercising its decision, nor can it be subjected to any review. It can reject the proposal [for additional bonds] for any reason or no reason. The addition of the referendum requirement is, we conclude, a severe impairment that defeats the expectations of the parties under their contracts. *See Allied Structural Steel Co. v. Spannaus,* 438 U.S. 234 (1978). (J.S. App. 15a.)

Finally, even if Washington's power of "governance" permits it to substitute a referendum for the Supply System's contractually guided decisions, its exercise does not excuse the Initiative's elimination of Bonneville from the decision making process. Bonneville's participation in Prudent Utility Practice decisions assures the bondholders that the projects cannot be

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[17] Appellant argues that Prudent Utility Practice is a meaningless standard. However, it is a recognized term in the industry (Akridge Dep. (CR 149), pp. 49-52), has been applied on other projects (Titmuss Dep. (CR 165), pp. 191-93), and has been applied by Bonneville to Projects 1, 2 and 3 (Hoberg Dep. (CR 144), pp. 34-35; Sienkiewicz Dep.(CR 142), p. 74). Moreover, as the court of appeals aptly noted,

> We need not attempt to define its contours. It is sufficient to note that it is the standard to which the parties agreed. (J.S. App. 4a, n.4)

terminated by unilateral action. Exs. 1, 2 (Project 1 and 2 Agree.), § 15(b); Ex. 4 (Project 3 Ownership Agree.), §§ 3, 4, 7. Initiative 394, however, permits voters residing within the governmental entities comprising the Supply System to decide that the projects will not be funded, without seeking Bonneville's consent. This elimination of multiparty participation in the most important decision relating to the projects is more than a simple change in the Supply System's governance.

D. THE DISTRICT COURT AND COURT OF APPEALS CORRECTLY DETERMINED THAT THE STATE COULD NOT JUSTIFY THE INITIATIVE.

Once a state law is shown to effect a substantial impairment, "the State, in justification, must have a significant and legitimate public purpose behind the regulation, *United States Trust Co.*, 431 U.S. at 22 . . ." *Energy Reserves Group, supra*, 51 U.S.L.W. at 4109. That justification will be sufficient only if the challenged legislation's

> adjustment of "the rights and responsibilities of contracting parties [is based] upon reasonable conditions and [is] of a character appropriate to the public purpose justifying [the legislation's] adoption." *United States Trust Co.*, 431 U.S., at 22. (*Id.*, 51 U.S.L.W. at 4109.)

The legislation must also be "necessary to serve an important public purpose." *United States Trust Co., supra*, 431 U.S. at 25. Applying precisely this standard, both the district court and the court of appeals correctly found that the Initiative was not justified.

1. The Court of Appeals Accorded the Appropriate Degree of Deference to the State's Legislative Judgment.

In reviewing the justification for the Initiative, the court of appeals noted that:

> Our determination whether the State's action is justified is affected by the fact that WPPSS is itself a political

> subdivision of the State, made up of other political subdivisions. . . . Because the State is a contracting party, we give less deference to its claims of justification for impairment. [*United States Trust Co.*] at 25-26. (J.S. App. 16a.)

This standard properly governed the court of appeals' inquiry. It is irrelevant that the State of Washington does not itself appear as a party to the contracts: in exercising its statutory authority, the Supply System, and its member municipal corporations, acted as "mere instrumentalities of the State."[18] *Meriwether v. Garrett,* 102 U.S. 472, 511 (1880); *see* J.S. 17, n.17. As this Court recently noted, it has "[i]n almost every case . . . held a *governmental unit* to its contractual obligations when it enters financial or other markets." *Energy Reserves Group, supra,* 51 U.S.L.W. at 4109, n.14 (citations omitted; emphasis supplied), *citing W. B. Worthen Co. v. Kavanaugh,* 295 U.S. 56 (1935) (State statute held to unconstitutionally impair obligations of a municipal corporation's bonds), *and* Note, "A Process-Oriented Approach to the Contract Clause," 89 Yale L.J. 1623, 1647-48 (1980) (distinguishing "public" from "private" contracts).

Strict scrutiny of legislation that impairs municipal contracts is necessary because "the State's self-interest is at stake." *United States Trust Co., supra,* 431 U.S. at 26. That rationale applies with particular force to the Supply System's obligations. The same voters ultimately responsible for selecting the Supply

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[18] In this sense, the Supply System must be distinguished from Kansas Power and Light, the utility whose contracts were impaired in *Energy Reserves Group, supra.* Although regulated by the Kansas Corporation Commission, KPL is not a governmental subdivision of a State, as is the Supply System. *See* 51 U.S.L.W. at 4109, n.14. Accordingly, the law affecting KPL's obligations did not implicate the State's self-interest. Here, on the other hand, Washington's electorate freed a governmental subdivision, which is composed of other governmental subdivisions, from its obligations to bondholders.

System's governing bodies participated in the passage of Initiative 394.[19] Furthermore, because the cost of Projects 1, 2 and 3 is recovered by Bonneville from all of its customers (Gjelde Aff. (CR 164), ¶ 6), nearly all Washington voters are economically affected by the projects. *See* PTO (CR 170)¶¶ 12-13 (describing Bonneville service area). Their self-interest was at stake in voting on the Initiative. Strict scrutiny is therefore imperative.

2. Permitting a Vote on Public Contractual Obligations Is Not a Legitimate Public Goal for Purposes of the Contract Clause.

Initiative 394's stated purpose is "to provide a mechanism for citizen review and approval of proposed financing for major public energy projects," including Projects 1, 2 and 3. Initiative, § 2 (J.S. App. 26a). Appellant thus suggests that the Initiative's primary public purpose is to provide a "citizens' vote" and that "[t]here is no less drastic means of accomplishing the goal of a citizens' vote than having a citizens' vote . . . ." J.S. 26.

Aside from the tautological nature of this argument, a citizens' vote is not a legitimate public goal for purposes of Contract Clause analysis. If it were, a State could avoid its contractual commitments at any time, without running afoul of the Contract Clause, simply by passing legislation calling for a referendum on whether to perform its obligations. Such a maneuver cannot be countenanced. The electorate had its say when it elected the representatives responsible for promulgating the Supply System's Bond Resolutions. It cannot be a legitimate public purpose to now permit it to decide whether the

[19] The Supply System is composed of 23 Washington municipal corporations, all governed by elected representatives. *See* RCW 54.12.010; 54.40.070 (providing for elections of PUD commissioners); RCW 35.17.020; 35.18.020; 35A.12.040; 35A.13.020 (providing for elections in towns and cities). Its Board of Directors is, in turn, chosen by "[t]he legislative body of each member" of the Supply System. RCW 43.52.370(1). The Supply System's Executive Board, created in 1981, is selected partially by the Board of Directors and partially by the Governor. RCW 43.52.374.

commitments contained in those Resolutions should be honored. *See Energy Reserves Group, supra,* 51 U.S.L.W. at 4109, n.14 ("When a State itself enters into a contract, it cannot simply walk away from its financial obligations.").

3. The District Court and Court of Appeals Correctly Concluded that the Initiative Is Not Reasonable in Light of Changed Circumstances.

State legislation cannot legitimately impair contractual rights in order to address problems existing at the time the contracts were entered into. *United States Trust Co., supra,* 431 U.S. at 31-32. To justify an impairment, there must be new circumstances that are not simply "changes . . . of degree . . . ." *Id.* at 32. Initiative 394 fails to surmount this hurdle, for the "concerns addressed by the Initiative were not unknown in the early 1970's." J.S. App. 20a.

The record amply supports this conclusion. Cost overruns had been recognized as concerns on nuclear projects by the 1970's. Sitzer Dep. (CR 188), pp. 152-53; *see also* Exs. 68 at 26, 69 at 1-3 (1967 and 1974 Reports of Atomic Energy Commission). Such problems have historically plagued large construction projects. Bates Dep. (CR 132), p. 49. The Supply System consequently addressed cost overrun and cost effectiveness concerns in the Prudent Utility Practice standard governing its actions on the projects. *See, e.g.,* Ex. 1 (Project 1 Agreement), § 1(p). As was true of the legislation considered in *United States Trust Co.,* then, the Initiative does not respond to concerns unknown at the time the contracts were executed.[20]

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[20] Furthermore, the Supply System's problems were largely ameliorated by the time of the Initiative's passage. The report of the Washington Senate Energy and Utilities Committee (Ex. 26), dated January 12, 1981, noted that the Supply System had appointed a new managing director in August of 1980, who had pledged to adopt a more rigorous approach to the Supply System's management. The Committee felt "encouraged" by his actions (Ex. 26, p. 4), and analysts subsequently agreed that the new director's policies largely resolved the Supply System's management problems. Hoberg Dep. (CR 144), pp. 42, 86; Titmuss Dep. (CR 165), p. 181. Indeed, in the ten months preceding April 1982, Projects 1, 2 and 3 proceeded approximately on schedule and close to the Supply System's budget. *See* Ex. 1 to Aff. of Alexander Squire (CR 156).

The Initiative is also unreasonable because it is not "tailored to the problems it was" purportedly enacted to solve. *See* J.S. 25, n.22. The Initiative states that it is intended to address concerns relating to the allocation of "limited financial resources." Initiative, § 2 (J.S. App. 26a). This purpose allegedly embraces the dual goals of requiring the Supply System to consider cost effectiveness criteria in making its decisions and forcing it to live within stated budgets. J.S. 27.

In providing for a public vote, however, the Initiative does not demand that the Supply System or the electorate consider the results of cost effectiveness studies. In fact, the only requirement for examination of cost effectiveness appears in the very contracts impaired by the Initiative, which mandate that decisions be made in conformity with Prudent Utility Practice. Nor does the Initiative require the Supply System to live within its budgets. It merely provides for a new citizens' vote whenever the Supply System wishes to exceed the spending authority established by any previous referendum approving the issuance of bonds.

4. The District Court and Court of Appeals Correctly Concluded That the Initiative Was Not Necessary to Serve Any Legitimate Public Purpose.

An enactment impairing contractual obligations can be justified only if it is "necessary" to serve an important public purpose. *United States Trust Co., supra,* 431 U.S. at 29. Accordingly, "a State is not free to impose a drastic impairment when an evident and more moderate course would serve its purposes equally well." *Id.* at 31. In this case, more moderate action than the Initiative could have remedied whatever problems confronted the Supply System.

For example, although the Senate Energy and Utilities Committee's Report is the basis for appellant's recitation of the Supply System's difficulties (*see* J.S. 23; *see also* Zemke Aff. (CR 159)), that Committee never recommended any measure similar to Initiative 394. Instead, it suggested ten steps to improve and oversee the Supply System's management. Ex. 27

at pp. 3-6. The State Legislature responded by enacting laws providing for better oversight and management of the Supply System. 1981 Wash. Laws (1st Ex. Sess.) Ch. 3, § 2; 1982 Wash. Laws (1st Ex. Sess.) Ch. 43, § 3. On the other hand, the Legislature in 1981 rejected bills calling for elections on Supply System bonds in certain circumstances (*See* Ex. 73), and Washington's Governor declared that Initiative 394 was "unnecessary." Ex. 72. The district court appropriately noted these rejections of the Initiative's solutions. RP 116. They leave little doubt that the Initiative was unnecessary, a conclusion reinforced by closer examination of its purported justifications.[21]

The Initiative was not necessary to assure public accountability. As the court of appeals noted, "[t]hrough the election process, the voters have always had direct or indirect control of" the Supply System (J.S. App. 17a), a fact admitted by the State. *See* State Defendants' Answer to Plaintiffs' Interrogatory No. 7 (Ex. 74). Furthermore, "[a]t least one alternative method of achieving public accountability has actually been adopted." J.S. App. 17a (citation omitted). That this alternative was enacted later is of no consequence, for it was available to the State at the time of the Initiative's passage.

Nor is the voter approval requirement necessary to assure consideration of cost effectiveness criteria:

> Cost effectiveness studies can be required without being tied to an election requirement for the issuance of bonds. . . . (J.S. App. 17a).[22]

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[21] In an effort to bootstrap its way past this Court's "necessity" requirement, appellant has defined the Initiative's purpose as the precise change which it accomplishes, arguing that there is no less drastic means of attaining that goal. Were this the appropriate mode of analysis, of course, every state enactment would be "necessary." It was clearly not this Court's intention, however, to create a meaningless standard. Moreover, requiring a vote on preexisting public obligations is not a legitimate public purpose. *See* Part D(2), *supra*.

[22] The Supply System recently agreed to submit to cost-effectiveness studies, in which the public will have the opportunity to participate, without a referendum on the issuance of additional bonds. *See* Addendum to Motion of Continental Illinois National Bank and Trust Company of Chicago to Dismiss or Affirm.

In fact, the Initiative does not require either the Supply System or the electorate to consider cost effectiveness. Instead, it gives the electorate the power, unburdened by any standard, to terminate funding of projects, a capability manifestly unrelated to cost effectiveness considerations.

Similarly, voters need not have the power to deny the Supply System authority to issue additional bonds in order to force adherence to budgets. The argument that the Initiative is necessary to serve this purpose hypothesizes that voters will approve issuance of additional bonds, thereby establishing a "debt limit." *See* J.S. 27-28. The Initiative, however, permits a complete rejection of funding authority for Projects 1, 2 and 3, a more drastic alternative than necessary to enforce budgets.

E. THE COURT OF APPEALS PROPERLY DECIDED THIS CASE WITHOUT REMANDING FOR FURTHER FINDINGS.

The district court's findings satisfy Fed. R. Civ. P. 52. The trial court adopted as findings 105 paragraphs of stipulated fact contained in the Amended Pretrial Order. RP 223. Directing its attention to the issues of disputed fact identified by the parties, the district court specifically found that the Initiative impaired the bondholders' contractual rights, reduced the security for their bonds, created uncertainty as to the Supply System's ability to finance completion of Projects 1, 2 and 3, and reduced the value of the bonds on the secondary market. RP 224 (J.S. App. 21a-22a). Accordingly, the district court concluded that the Initiative effected a "substantial impairment." RP 225 (J.S. App. 22a). Finally, the trial court stated that it could not "find that 394 is reasonable and necessary under the guidelines . . . set forth in the *United States Trust* case." RP 226 (J.S. App. 23a). In light of the nature of the

case, largely involving the construction of contracts and statutes, more extensive findings were unnecessary. [23]

Moreover, "it is settled that findings are not jurisdictional and the appellate court may decide the appeal without further findings if it feels that it is in a position to do so." C. Wright & A. Miller, *Federal Practice and Procedure*, § 2577, pp. 699-700 (1971). The court of appeals considered the findings sufficient to enable it to review the district court's decision. Because the results of its review were manifestly correct, it would be pointless to consume valuable judicial resources by remanding for further findings.

F. APPELLANT LACKS STANDING TO INVOKE THIS COURT'S APPELLATE JURISDICTION.

Appellant is a self-appointed "citizens' group that drafted and campaigned for" Initiative 394. J.S. 3. Its participation in the political process leading to the adoption of the Initiative, however, does not give it the direct personal stake in the outcome of this litigation that would permit it to invoke this Court's appellate jurisdiction. *See* Motion of Appellee Continental Illinois National Bank and Trust Company of Chicago to Dismiss or Affirm.

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[23] Neither the district court nor the court of appeals entered findings as to the meaning of Prudent Utility Practice. *See* J.S. 29. Such findings were unnecessary because Prudent Utility Practice, a contractually defined term, "is the standard to which the parties agreed." J.S. App. 4a, n.4. Furthermore, at the time the district court entered its findings, counsel for the State of Washington, referring to counsel for the appellant in this Court, twice advised the court that the findings were sufficiently specific for purposes of appeal. RP 226-228. No party requested written findings or moved for additional findings.

CONCLUSION

For the reasons stated above, this Court should dismiss the appeal or, in the alternative, summarily affirm the decision of the court of appeals.

Respectfully submitted,

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